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SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER
NOVEMBER 12, 2004 ISSUE

1. Summary. Each week, AMEmbassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:

- Manufacturing Growth for Eighth Consecutive Month;
- Rise in Individual Credit Debt Unsustainable;
- Reserve Bank Increases Foreign Exchange and Gold Reserves;
- Real Wholesale Trade Sales Increase 18.1 Percent;
- Provincial Governments Project R2.2 Billion Deficit;
- September House Prices Increase 33.9 Percent; and
- Economic Inequalities Still Remain.

End Summary.

MANUFACTURING GROWTH FOR EIGHTH CONSECUTIVE MONTH

2. According to Statistics South Africa (StatsSA), manufacturing production grew by 6.1 percent (y/y) in September compared to August's 6.8 percent growth. September's manufacturing sales grew by 12 percent. Third quarter 2004's manufacturing production grew by 2.7 percent (seasonally adjusted) compared to second quarter 2004's 1.8 percent growth. Third quarter growth was robust with eight out of ten manufacturing sub-sectors reporting higher growth. The main contributors to third quarter growth were the food, motor vehicle and furniture sectors. Strong domestic consumption was the key reason behind manufacturing growth, as the Euro zone's growth has not been as strong as initially expected. Approximately 30 percent of South Africa's manufactured goods are exported, and of these exports, roughly 35 percent go to the Euro zone. Continued strength of the rand and uncertain global oil prices constrain domestic producers from raising their prices. Source: Standard Bank, Manufacturing Unpacked, November 9; Business Day, Business Report, November 10.

3. Comment. There are signs of manufacturing growth leveling off in the near future. The Investec Purchasing Manager's Index declined in October, (although it is still above the 50 level, which signals activity expansion) and the rand has recently strengthened. During October 2004, the rand appreciated 2.5 percent, while the average monthly change in 2004 so far is a 0.3 percent appreciation. Lower than expected global growth may also contribute to a possible slowdown in manufacturing activity. ABSA economist John Loos believes that consumer demand peaked in the third quarter and predicts consumers to curtail future spending. Healthy growth is still expected for manufacturing though lower than the current 6 percent monthly growth. Manufacturing contributes 18 percent to South Africa's economy and continuing expansion in this sector is needed for sustained economic growth. End Comment.

RISE IN INDIVIDUAL CREDIT DEBT UNSUSTAINABLE

4. Efficient Research financial services group contents that South African credit debt levels are manageable, but current growth rates cannot be supported. Total credit card debt in September 2004 was R3 billion (\$500 million using 6.1 rands per dollar) higher than the previous September, with individuals accounting for most of the increase. The amount owed on individual credit cards is at the highest level yet at R18 billion (\$3 billion). Overall, total South African credit increased by R9.5 billion (\$1.6 billion) in September compared to August 2004. However, the use of overdrafts by individuals declined, indicating that savings on lower home (all of South African mortgages issued use variable rates) and vehicle loan rates were sources of financing increased individual credit. Increased use of overdrafts is one indication of credit overextension. Source: Business Report, November 10.

RESERVE BANK INCREASES FOREIGN EXCHANGE AND GOLD RESERVES

15. The South African Reserve Bank (SARB) increased foreign exchange reserves, reaching US \$11.3 billion in October from \$10.7 billion in September and \$10.4 billion in August. Gold reserves of \$1.7 billion lifted total gross reserves to \$13 billion at the end of October. In October, SARB bought \$590 million worth of foreign exchange and provided \$372 million worth of financing for repayment of a National Treasury euro-denominated loan. Many economists believe that the SARB should have at least \$20 billion in foreign exchange reserves given that average monthly imports have exceeded \$4 billion this year. From 1999 through February 2004, the foreign exchange reserves had fluctuated around the \$6 billion level. In March 2004, reserves increased by \$2 billion and have been increasing ever since. Source: I-Net Bridge, November 5; Business Day, November 8.

REAL WHOLESALE TRADE SALES INCREASE 18.1 PERCENT

16. According to Statistics South Africa (StatsSA), August real wholesale trade sales, excluding diamonds, increased 18.1 percent (y/y) compared to June and July growth of 16.7 percent and 10.6 percent, respectively. The three months' (ending in August) seasonally adjusted real wholesale trade sales increased 15.1 percent (y/y), as wholesale inflation remained around 2 percent. In May 2004, StatsSA revised the company list that comprises wholesale and retail trade data, saying that sales were systematically under reported. The new list, based on the value-added tax (VAT) database obtained from the South African Revenue Service (SARS), covers all businesses in South Africa expecting to reach sales of R300,000 (\$50,000) for a 12-month period. The coverage of the new company list is greater than that of the old list. Company information is provided by SARS and verified by StatsSA. StatsSA has further plans to improve company coverage by accessing corporate income tax records. Source: I-Net Bridge, November 5.

PROVINCIAL GOVERNMENTS PROJECT R2.2 BILLION DEFICIT

17. Provincial governments are projecting a R2.2 billion deficit (\$361 million using 6.1 rands per dollar) in expenditure in the FY2004, largely due to unexpectedly high increases in the number of people receiving foster care and disability grants. Those provinces not having surplus funds will have to finance these deficits from next year's budgets, as the national government's policy is to not fund overruns of provincial budgets. In the Medium-Term Budget Policy Statement, Finance Minister Manuel announced an additional R4.3 billion (\$705 million) provincial appropriation for FY2004; however, the projected aggregated R2.2 billion budget deficit takes this into account. The Eastern Cape and Northern Cape provinces are already operating on overdrafts, while some provinces have already instituted cost containment measures and other initiatives to ensure their deficits are reduced to levels of available funding. Provincial revenue this fiscal year included budgeted equitable share spending not earmarked of R160 billion, conditional grants of R21.2 billion and provincial revenue of R5.4 billion. The figures on provincial spending for the first six months of this fiscal year also showed slow spending of capital expenditure. Provinces spent 29.5 percent (R3.3 billion) of their R11.3 billion capital budgets. Capital spending in education was 23.2 percent and provinces spent 27.2 percent in health capital spending. The lowest rates of capital spending were in Gauteng (6.4 percent), Mpumalanga (11.9 percent) and Northern Cape (12.3 percent); Free State and Limpopo recorded the highest at 48.1 percent and 54.6 percent, respectively. Provinces spent 52 percent of their R47.3 billion social development budget by the end of September. Provincial spending on social development rose from R20.9 billion in 2000-01 to R42.4 billion in 2003-04, an annual average nominal growth of 26.6 percent. Source: Business Day, November 8.

SEPTEMBER HOUSE PRICES INCREASE BY 33.9 PERCENT

18. Real house prices increased by 33.9 percent this year through September, compared with a revised increase of 33.3 percent through August, according to the latest ABSA bank house price index. Monthly house price increases were on a declining trend, from 3.1 percent in January to 1.5 percent in September, indicating potential lower growth in the near future. Relatively stable interest rates this year, combined with the continuing rise in house prices, already resulted in an increase in new mortgage payments. Ultimately, rapidly growing housing prices will increase housing costs leading to lower demand for housing and lower growth in prices. The ABSA bank

house price index showed a nominal year-on-year increase of 35.4 percent in house prices in October and the revised increase of 35.6 percent for September, with the y/y increase in the past 10 months averaging 32 percent. Source: IOL, November 8.

ECONOMIC INEQUALITIES STILL REMAIN

19. The Economic Transformation Audit and Scorecard, compiled by a panel of economic experts for the Institute for Justice and Reconciliation, showed poverty and inequality are still increasing in South Africa. The Institute's calculations show that 58 percent of the South African population and 69 percent of black South Africans now live under the basic poverty level. Between 1996 and 2001, the study found that with poverty measured in terms of income increased, more households fell below the basic poverty line of R250 (\$40) a day. Those living under the mean (average) poverty line of R91 (\$15) a day rose from 26 percent in 1996 to 28 percent in 2001, while black South African per capita income as a percentage of white income declined by 1.3 percent from the already low base of 8.2 percent in 1996. The average black South African now has less than seven percent of the income of an average white South African. White and Asian shares of the total income are growing again after a slight drop, but the average white person is somewhat worse off, indicating more poverty as well as wealth. Real household income at the higher end of the income spectrum increased (in all population groups), resulting in a widening in inequality for the first time since 1975. Income of households headed by South African women relative to those headed by men increased by 4 percent since 1996. The percentage of households with clean water and electricity increased since 1996, although up to one third of the population is still without these basic services. The percentage of families living in permanent structures decreased from 77.6 percent in 1995 to 73.8 percent in 2002, and the number of households increased during the same period. Between 1995 and 2002, the percentage of children at school decreased by 0.7 percent and the infant mortality increased by 14 percent. The number of jobs increased by 1 million during the same time frame, however, due to a large increase in the labor force, unemployment is now at 42 percent. Source: Sunday Argus, November 7.

FRAZER